BEFORE THE PUBLIC UTILITIES COMMISSION

OF THE STATE OF CALIFORNIA

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Application of San Diego Gas & Electric Company (U 902 G) and Southern California Gas Company (U 904 G) to Recover Costs Recorded in their Pipeline Safety and Reliability Memorandum Accounts.	Application 14-12-016 (Filed December 17, 2014)

REPLY OF SAN DIEGO GAS & ELECTRIC COMPANY (U 902 G) AND SOUTHERN CALIFORNIA GAS COMPANY (U 904 G) TO THE COMMENTS OF THE OFFICE OF RATEPAYER ADVOCATES, THE UTILITY REFORM NETWORK, AND SOUTHERN CALIFORNIA GENERATION COALITION ON THE SEPTEMBER 9, 2016 PROPOSED DECISION

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Pursuant to Rule 14.3(d) of the Rules of Practice and Procedure of the California Public Utilities Commission ("Commission"), San Diego Gas & Electric Company ("SDG&E") and Southern California Gas Company ("SoCalGas") (jointly, "Applicants") respectfully submit their Reply to the Comments of the Office of Ratepayer Advocates ("ORA"), The Utility Reform Network ("TURN"), and Southern California Generation Coalition ("SCGC"); together with TURN and ORA, "Intervenors") on the September 9, 2016 Proposed Decision ("PD"). In opening comments, Intervenors urge the Commission to abate the precedential value of its resolution of this first PSEP after-the-fact reasonableness review[1] and challenge the legal and factual basis of the PD.[2] In so doing, Intervenors ignore not only the benefits of the precedential value of the Commission's decision – including providing clarity, guidance, and promoting cost efficiency – but also the substantial evidence presented by Applicants and relied upon by the PD. The underlying record evinces that costs were incurred reasonably and Applicants were reasonable managers in promptly undertaking the massive work ordered by the Commission to enhance the safety and reliability of Applicants' natural gas pipeline transmission systems. As such, the PD correctly finds that the majority of costs presented for review and recovery are

[1] TURN/SCGC Comments at 1.
[2] ORA Comments at 1.

reasonable[3] and that Applicants reasonably and prudently executed this State and Commission-ordered safety enhancement work.[4]

I. THERE IS AMPLE EVIDENTIARY SUPPORT IN THE RECORD FOR THE FINDINGS IN THE PD.

Ignoring the record,[5] Intervenors argue that the evidence does not support the PD's findings that the costs granted were reasonable, and thus the PD should have no precedential value[6] and/or all findings of reasonableness should be deleted from the PD.[7] Intervenors' recommendations should be disregarded for several reasons: (i) the Commission used the correct standard of review in employing the preponderance of the evidence standard rather than clear and convincing evidence[8]; (ii) the record provides sufficient evidence in accordance with the preponderance of the evidence standard to support the PD's findings of reasonableness[9]; (iii) the

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[3] Applicants' Opening Comments address the PD's findings related to PSEP-specific insurance overhead costs.

[4] PD at 51 (Conclusion of Law 51) and 54 (Ordering Paragraphs 3 and 4).

[5] TURN/SCGC also ignore the record in complaining that the PD largely is "lifted word for word" from Applicants' Opening Brief. (TURN/SCGC Comments at 2). This over-simplification belies the fact that the statements in the Applicants' Opening Brief and the PD are supported amply by the evidence composing the underlying record.

[6] TURN/SCGC Comments at 5; ORA Comments at 1.

[7] ORA Comments at 1.

[8] Contrary to ORA's apparent assertion that clear and convincing evidence is the correct standard, the PD and the Commission's precedent are clear that the correct standard is a preponderance of the evidence. ORA Comments at 2; PD at 8; D.14-06-007, mimeo., at 7-8, 51.

[9] Specifically, ORA complains the following precludes a finding of reasonableness. However, as explained in turn, each of ORA's concerns is based on selective review of the record or misinterpretation of the PD.

(a) Applicants failed to compare revised project estimates with actual costs. (ORA Comments at 4; ORA Opening Brief at 9-10).
- This assertion ignores Applicants' explanations of the purpose of estimates, why a comparison was not always possible, the fact that comparisons were in fact made in certain instances, and that such comparisons are not necessary to determine reasonableness. (*See* Applicants' Reply Brief at 15-21). Further, Applicants provided ample evidence that they have acted reasonably and prudently. (*See* Applicants' Opening Brief at 33-54 and Reply Brief at 4-15).

(b) Applicants did not explain why actual project spending exceeded estimates (ORA Comments at 4-5).
- Again, such an explanation is not necessary to satisfy the reasonable manager standard. (Applicants' Reply Brief at 15-21). Regardless, the record contains explanations for why estimates were exceeded in certain instances. (*See, e.g.*, Ex. SCG-09 (Mejia) at 34-36). Indeed, the PD cites the explanations for the increases. (*See*, *e.g.*, PD at 23.)

(c) Applicants did not make a showing that they met industry best practices, let alone followed their own protocol regarding comparing project estimates with actual spending (ORA Comments at 4-5).

minimum requirements set forth in Decision ("D.") 14-06-007 are not regarded by Applicants as the only required showing for a finding of reasonableness (indeed, in most instances Applicants have made a showing in excess of the stated minimum requirements, evidencing that the minimum requirements are not deemed to affect Applicants' burden to establish reasonableness[10]); and (iv) particularly during this nascent stage of Pipeline Safety Enhancement Plan ("PSEP") after-the-fact reasonableness reviews, Commission precedent provides invaluable guidance to Applicants going forward and promotes clarity, certainty, consistency, and cost-efficiency.

II. IT IS APPROPRIATE FOR THE COMMISSION TO PROVIDE GUIDANCE TO APPLICANTS REGARDING USE OF THE PERFORMANCE PARTNERSHIP PROGRAM.

Intervenors oppose the PD's finding that Applicants' Performance Partnership Program ("PPP") is a reasonable means to engage construction contractors because PPP was not utilized by Applicants in the three projects for which a determination of reasonableness currently is sought.[11] D.14-06-007, however, authorizes Applicants to "file for preapproval of specific

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- Here, ORA conflates two separate issues and associates industry best practices with a comparison of estimates to actuals. Although Applicants provided explanations for why estimates were exceeded in certain instances, such a showing is not a prerequisite to demonstrating reasonableness. Moreover, Applicants provided ample evidence that they have acted reasonably and prudently. (*See* Applicants' Opening Brief at 33-54 and Reply Brief at 4-15).

(d) The PD relies solely on ORA's accuracy audit in support of finding costs reasonable (ORA Comments at 7-8).
- ORA misconstrues the PD, which explicitly acknowledges that ORA's audit was merely a "determination of accuracy" and that the costs at issue were deemed reasonable because "the majority of the costs were subject to competitive bidding and negotiations." (PD at 21 and 26).

(e) The PD relies solely on the Commission's January 2012 Technical Report in concluding PMO costs are reasonable. (ORA Comments at 5-6).
- Again, ORA's protest is based on a misreading of the PD, which cites to the record in support of finding the PMO costs reasonable and recites at least nine reasons the PMO is important; only then does the PD supplement previous recitations to quote the technical report as underscoring its finding. (PD at 31-32). Further, although SCGC recommends a disallowance because SoCalGas and SDG&E chose to use contractors to augment internal resources, no other party challenged the PMO function, or proposed or supported disallowances.

[10] *See, e.g.,* Applicants' Opening Brief at 18 (referencing Ex. SCG-01 (Phillips); Ex. SCG-02 (Phillips); Ex. SCG-03 (Phillips); Ex. SCG-04 (Phillips); Ex. SCG-07 (Mejia); Ex. SCG-08 (Mejia); and Ex. SCG-09 (Mejia)); *see also* A.14-12-016, mimeo., at 6-7.

[11] ORA Comments at 6-7; TURN/SCGC Comments at 8-9.

projects seeking approval of a cap or for other specific guidance."[12] A finding regarding the reasonableness of PPP is necessary at this time to avoid uncertainty and put to rest TURN's and SCGC's opposing arguments that Applicants should be required to solicit competitive bids for each item of construction work instead of using PPP.[13] Without a determination now, Applicants will have no clarity on their use of PPP. Accordingly, rather than leaving ambiguity until a future after-the-fact reasonableness review as to whether the Commission approves of the use of PPP, the Commission, consistent with D.14-06-007, should provide guidance regarding the reasonableness of engaging construction contractors for future PSEP work using the PPP.[14]

III. APPLICANTS REMOVE EXECUTIVE INCENTIVE COMPENSATION IN ACCORDANCE WITH D.14-06-007.

TURN/SCGC reiterate arguments that Applicants have failed adequately to address D.14-06-007's requirement to remove Executive Incentive Compensation.[15] This ignores the fact that SoCalGas and SDG&E generally do not allocate executive compensation costs to PSEP. However, in the rare event executive compensation is included, SoCalGas and SDG&E manually remove the component of the executive compensation associated with incentive compensation.[16]

IV. COMPETITIVE BIDDING.

TURN/SCGC request the Commission to make additional findings regarding competitive bidding that not only contravene prior Commission decisions[17] but also fail to consider the additional support Applicants provided for the incurred costs.[18] The Commission previously has found that competitive bidding provides a good indication of market prices and supports a finding of reasonableness of the resulting cost.[19] Moreover, Applicants did not rely solely on

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[12] D.14-06-007, mimeo., at 2.
[13] Ex. SCGC-TURN-01 (Yap) at 2.
[14] Applicants' Opening Brief, pp. 26-27.
[15] TURN/SCGC Comments at 9-11.
[16] *See* Applicant's Reply Brief at 38-39. To illustrate the process, in A.16-09-005, Applicants included a small amount of executive compensation incurred for PSEP ($773). To comply with the directives to remove executive incentive compensation, Applicants manually removed $189. In other words, Applicants calculated the disallowance based on the executive compensation charged directly to PSEP.
[17] *See, e.g.*, D.09-06-027, mimeo., at 47.
[18] TURN/SCGC Comments at 6-8.
[19] D.09-06-027, mimeo., at 30; *see also* D.00-07-020, mimeo., at 137.

competitive bidding to support the reasonableness of the incurred costs. Indeed, Applicants provided extensive testimony detailing the project costs, explaining which materials and services were competitively bid, why certain contractors or materials were not competitively bid, and the need for company labor and expense.[20]

V. CLARIFICATION OF REVENUE REQUIREMENT.

TURN/SCGC seek to reduce the revenue requirement stated in the PD by the amount disallowed by the PD*, i.e.,* by the $2.181 million sought by Applicants for PSEP-specific insurance overhead costs.[21] As noted in Applicants' Opening Comments,[22] the PSEP-specific insurance overheads should be adjusted to total approximately $1.961 million instead of the originally stated $2.181 million.[23]

Respectfully submitted,

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[20] *See, e.g.*, Ex. SCG-09 (Mejia) at 18-40.
[21] TURN/SCGC Comments at 11.
[22] *See* SoCalGas and SDG&E Opening Comments at 7-9.
[23] If the PD is modified and the PSEP-specific insurance overheads are authorized for recovery, SoCalGas' revenue requirement should be $26.60 million. Alternatively, if cost recovery is denied (with or without prejudice) SoCalGas' revenue requirement should be lowered to $24.86 million. (*See* SoCalGas and SDG&E Opening Comments at 10 and Appendices A-B).